

MEMO# 3036

August 21, 1991

NASD NOTICE ON USE OF "NEGATIVE RESPONSE" LETTERS IN SWITCHING CUSTOMERS FROM ONE MUTUAL FUND TO ANOTHER

August 21, 1991 TO: SEC RULES COMMITTEE NO. 48-91 RE: NASD NOTICE ON USE OF "NEGATIVE RESPONSE" LETTERS IN SWITCHING CUSTOMERS FROM ONE MUTUAL FUND TO ANOTHER _____ In its June Notice to Members, the NASD reminded members of the requirements governing the use of "negative response" letters, i.e., letters which recommend that customers switch from one mutual fund to another and state that if the customer does not respond by a specific date, the exchange will be executed automatically (the negative response feature). A copy of the NASD Notice is attached. The NASD reminded members who engage in this practice that, in addition to the suitability, prospectus delivery, and disclosure requirements governing such recommendations, no member may exercise discretion in a customer's account without obtaining prior written authorization from the customer. Thus, a member may not switch a customer from one fund to another based on the lack of a response, unless the member has on file prior written authorization permitting the member to exercise discretion in the account. Several members have expressed concern that the NASD's position could be interpreted to include "sweep" arrangements. However, it is our understanding that historically the NASD has not considered the authority to "sweep" a customer's funds into a money market fund to be investment discretion. Moreover, it appears that it would be impractical to require written authorization under these arrangements. Accordingly, the Institute is considering requesting an exception for "sweep" arrangements from the NASD's position expressed in the Notice. Please provide me with any comments you have on the NASD's position on "negative response" letters or that you would like included in the Institute's letter requesting an exception for "sweep" arrangements by September 6, 1991. My direct number is 202/955-3523. Amy B.R. Lancellotta Assistant General Counsel
Attachment